

# Financial Markets



**Irving Trust**

Irving Trust Company  
One Wall Street  
New York, NY 10015

**Economic Research &  
Planning Division**

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Recent events have given the market reason to be more optimistic about prospects for interest rate declines. The economy as well as the monetary aggregates are showing signs of slowing their rapid pace of growth. Yet, there is a dark side to the good news. Harsh March weather may be contributing to the weakness in the economic numbers. Other special factors, particularly those related to the (then) approaching April tax deadline, may have distorted the March monetary data. Credit growth remains rapid and above target. But the glimmer of hope remains.

The monetary aggregates are showing signs of slowing: In February, M1 grew at a 6.7% annual rate; March saw this drop to a 5.5% rate. Similarly, M2's growth has slowed, but more sharply, from 8.6% to 3.5%. M3's heated pace of 10.1% in February has cooled to 8.4% in March. In terms of its long-run target, M1's 6.9% growth from its November-centered target base is within its 4%-8% band. M2's growth at 6.4% is close to its lower band of 6% and well off its 9% target top. M3 alone is near its targeted maximum rate (of 9%), growing at an 8.7% clip from its November-centered base. In terms of its weekly target, M1's performance is much more dramatic: It fell from just one-tenth of \$1 billion below the top of its target to be just \$2 billion above its target bottom--in one week! But money growth can be erratic. What can we tell from these statistics?

First, note that the slowing is spread across the aggregates, M1 through M3. Next, remember that money growth can be a good leading indicator. Monetarists believe this because they think that money is a prime causal factor. I reject this emphasis. But I encourage an interpretation of the short-term monetary data as being "money demand data" rather than "money supply data." After all, the Fed controls the quantity of reserves in the banking system on a week-to-week basis, not the quantity of money--that's the result of demand forces. Reserves can support different amounts of money (M1, M2, or M3), depending on how depositors choose to hold their money balances: As currency? As demand deposits? As CDs? As MMDA deposits? Depending on deposit preferences, different amounts of reserves are absorbed (and money "supplied").

As income growth slows, depositors tend to hold fewer balances of all types. Thus a slowing in "money" might be the harbinger of a slowing in economic growth. Slower money growth therefore may stem from an incipient slowing in the economy rather than from a capricious shift in depositors' preferences for money.

Money demand relationships are notoriously fickle. Statistical efforts to explain and predict wiggles in money demand fail if the objective is to be able to understand all the short-term determinants of those demands. But in the first quarter, we know nominal GNP is growing fast (about a 12% rate). Even so, M1 is within its target range, growing at a 7.5% rate, quarter over quarter. This means M1's velocity is rising at a 4.5% rate (12.0% minus 7.5%)--quite rapid. The decline in M1's growth rate may mean a further increase in M1's already fast growing velocity (possibly a demand shift). Alternatively, it may signal that nominal GNP is slowing its growth. The widespread slowing of the aggregates makes more reliable the conclusion that it's the economy that's slowing. There is reason to be optimistic on interest rates, but also to be cautious.

Robert A. Brusca



# Irving Trust

## Market Yields

|                                                            | 4/13/84 (Noon) | Week Ago | Year Ago |
|------------------------------------------------------------|----------------|----------|----------|
| <b>Prime Lending Rate at Irving Trust Company</b>          | 12.00          | 12.00%   | 10.50%   |
| Effective since                                            | 4/5/84         |          |          |
| <b>Discount Rate at Federal Reserve Bank</b>               | 9.00           | 8.50     | 8.50     |
| <b>Federal Funds</b>                                       | 10.19          | 10.38    | 8.63     |
| <b>Repurchase Agreements</b>                               | 10.10          | 10.38    | 8.63     |
| <b>U.S. Treasury Issues</b>                                |                |          |          |
| <b>Bills</b>                                               |                |          |          |
| 3 months                                                   | 10.06          | 10.07    | 8.39     |
| 6 months                                                   | 10.41          | 10.49    | 8.69     |
| 1 year                                                     | 10.74          | 10.78    | 8.93     |
| <b>Coupons</b>                                             |                |          |          |
| 2 years                                                    | 11.47          | 11.55    | 9.49     |
| 4 years                                                    | 12.00          | 12.11    | 9.86     |
| 7 years                                                    | 12.34          | 12.45    | 10.21    |
| 10 years                                                   | 12.41          | 12.53    | 10.32    |
| <b>Long Bond</b>                                           | 12.45          | 12.57    | 10.38    |
| <b>Negotiable Certificates of Deposit-Secondary Market</b> |                |          |          |
| 1 month                                                    | 10.15          | 10.30    | 8.55     |
| 3 months                                                   | 10.30          | 10.35    | 8.55     |
| 6 months                                                   | 10.60          | 10.60    | 8.70     |
| 1 year                                                     | 11.15          | 11.25    | 9.10     |
| <b>Banker's Acceptances</b>                                |                |          |          |
| 1 month                                                    | 10.33          | 10.42    | 8.60     |
| 3 months                                                   | 10.56          | 10.61    | 8.60     |
| 6 months                                                   | 10.87          | 10.86    | 8.70     |
| <b>Eurodollar Deposits</b>                                 |                |          |          |
| 1 month                                                    | 10.63          | 10.81    | 9.00     |
| 2 months                                                   | 10.69          | 10.88    | 9.13     |
| 3 months                                                   | 10.88          | 10.93    | 9.13     |
| <b>Commercial Paper - Prime Names</b>                      |                |          |          |
| Directly placed by:                                        |                |          |          |
| <b>Finance Companies</b>                                   |                |          |          |
| 1 week                                                     | 10.21          | 10.41    | 8.76     |
| 1 month                                                    | 10.28          | 10.48    | 8.68     |
| 3 months                                                   | 10.40          | 10.40    | 8.81     |
| <b>Bank Holding Companies</b>                              |                |          |          |
| 1 month                                                    | 9.71           | 9.71     | 8.68     |
| <b>Dealer Placed:</b>                                      |                |          |          |
| 3 months                                                   | 10.56          | 10.65    | 8.78     |
| <b>New AA Corporate Utility Bond</b>                       | 13.50          | 13.70    | 11.65    |
| <b>Tax Exempt</b>                                          |                |          |          |
| 6 month Project Notes                                      | 5.55           | 5.60     | 4.60     |
| 1 year AAA Bond                                            | 5.75           | 5.75     | 4.75     |
| 5 year AAA Bond                                            | 7.40           | 7.40     | 6.50     |
| 20 year AAA Bond                                           | 9.40           | 9.70     | 8.25     |

This information represents prevailing market yields.

**It should not be construed as an offering.**

All yields are on the offered side of the market.

Cable Address:

"IrvingBank" Telex: I.T.T. 420268 • R.C.A. 232241

W.U.I. 62832 • French 82629